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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1931

No. 582

WOOLFORD REALTY COMPANY, INC., PETITIONER,

v.

J. T. ROSE, COLLECTOR OF INTERNAL REVENUE FOR THE DISTRICT OF GEORGIA

PETITION FOR A WRIT OF CERTIORARI TO THE CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT, AND BRIEF IN SUPPORT THEREOF

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J. T. ROSE, COLLECTOR OF INTERNAL REVENUE FOR THE DISTRICT OF GEORGIA

PETITION FOR WRIT OF CERTIORARI

May it Please the Court:

The petition of Woolford Realty Company, Inc. respectfully shows to this Honorable Court:

A

SUMMARY STATEMENT OF THE MATTER INVOLVED

Petitioner sued the Respondent to recover certain Federal income taxes alleged to have been erroneously and illegally collected. Petitioner's declaration showed the following facts (R. 2-6):

Petitoner and Piedmont Savings Company are separate corporations. They were not affiliated in 1925 and 1926, but were affiliated throughout 1927 through the ownership by Petitioner of 96% of the stock of Piedmont Savings Company. The corporations filed separate returns for 1925 and 1926, but filed a consolidated return for 1927 under Section 240 of the Rev-

enue Act of 1926,[1] which return was accepted by the Commissioner. In computing the consolidated net income of the group for 1927 for income tax purposes, the Commissioner of Internal Revenue has taken into consideration the deductions allowable to each of the members of the group under Section 234 of the Revenue Act of 1926, but the Commissioner has refused to allow as deductions claimed under Section 206 of that Act, the amounts of certain statutory "net losses" (as defined in Section 206) sustained by Piedmont Savings Company in the years 1925 and 1926. Upon this basis the Commissioner has determined a consolidated net income of $36,133.82, and income taxes have been assessed and paid on this amount.

It is not disputed that the statutory "net losses," referred to above, were sustained by Piedmont Savings Company in the amount of $43,478.25 in 1925 and in the amount of $410.82 in 1926, or in a total amount for the two years of $43,889.07. Petitioner claims that the amount of these statutory "net losses" should be allowed as deductions in the computation of consolidated net income for 1927. If such deductions are allowed, the aggregate of allowable deductions would have exceeded the aggregate gross income, and no income tax would be payable under the consolidated return. A claim for refund was filed and suit was brought for the recovery of the income taxes thus paid for 1927.

The District Court sustained Defendant's general demurrer to the declaration, and on appeal the Circuit Court of Appeals for the Fifth Circuit affirmed the judgment of the District Court.

The Circuit Court of Appeals took the position "that the statutory net loss deduction was personal to the taxpayer sustaining it and could be availed of in the following year by that taxpayer alone, and by him only to the extent that he had net

[1]Pertinent statutory provisions and Treasury Regulations are quoted in full in an appendix to the brief in support of this petition.

income in that year."[2] The learned Judge apparently means by "net income" the amount by which gross income exceeds the deductions allowable under Section 234(a) and is of the opinion that where these deductions exceed gross income there is no net income. Since in 1927 the gross income of Piedmont Savings Company was exceeded by the deductions allowable to Piedmont Savings Company under Section 234 of the Revenue Act of 1926, the Court held that Piedmont Savings Company had no "net income" and that therefore its "net losses" for the two preceding years were not deductible and should be disregarded in the computation of consolidated net income.

B

REASONS RELIED ON FOR THE ALLOWANCE OF THE WRIT

1. The Circuit Court of Appeals has herein decided an important question of Federal Law which has not been, but should be, settled by this Court. The question is whether a statutory "net loss" incurred by a corporation in one year may be used to reduce the consolidated net income of an affiliated group, of which such corporation is a member, in another year in which the corporation which has sustained the "net loss" has, without consideration of the "net loss," no separate "net income" of a plus quantity. The Board of Tax Appeals and the lower Federal Courts have already decided numerous cases[3] involving this

[2]The quotation is from the opinion of the Circuit Court of Appeals for the Fifth Circuit in the case of *Planters' Cotton Oil Co., Inc. v. Hopkins*, decided November 20, 1931, where the Court describes its holding in the case at bar.

[3]*National Slag Co. v. Commissioner*, 47 F. (2d) 846 (C. C. A. 3rd, 1931); *Commissioner v. Ben Ginsburg Co.*, Unreported (C. C. A. 2nd, November 2, 1931); *Planters' Cotton Oil Co., Inc. v. Hopkins*, Unreported (C. C. A. 5th, November 20, 1931); *s. c.* 47 F. (2d) 659 (N. D. Tex. 1931); *Alabama By-Products Corporation*, 18 B. T. A. 919; *Ginsburg Co.*, 19 B. T. A. 81; *Buckie Printers' Ink Co.*, 19 B. T. A. 943; *Pittsburgh Gasoline Co.*, 21 B. T. A. 297; *General Box Corporation*, 22 B. T. A. 725; *Arrow Coal & Ice Company*, 22 B. T. A. 1341; *Tolerton & Warfield Company*, 23 B. T. A. 892; *Hawley Investment Company*, 23 B. T. A. 953; *Small's, Inc.*, 24 B. T. A. __; *Abelson Realty Company, Inc.*, 24 B. T. A. __; *Summerfield Co.*, 24 B. T. A. __.

question, and undoubtedly hundreds of other cases are still pending before the Bureau of Internal Revenue, the Board of Tax Appeals and the Courts. It is most important, therefore, that this Court settle the question and put an end to the uncertainty and confusion which is causing such widespread dispute before the Courts, the Board of Tax Appeals and the Bureau of Internal Revenue.

2. The decision rendered by the Circuit Court of Appeals in this case is in conflict with the decision of the Circuit Court of Appeals for the Third Circuit in the case of *National Slag Co. v. Commissioner of Internal Revenue*, 47 F. (2d) 846 (1931)[4].

3. The Circuit Court of Appeals has disregarded the clear and repeated holdings of this Court to the effect that the rule requiring adherence to the letter of a statute applies with peculiar strictness to taxing acts and to the effect that such statutes are not to be extended by implication beyond the clear import of the language used and must in all cases of ambiguity be construed most liberally in favor of the taxpayer[5].

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[4]The decision in the case at bar is also in conflict with all of the decisions of the Board of Tax Appeals cited in the preceding footnote. The case of *Summerfield Co.*, there cited, was decided by the Board after its attention had been called to the conflicting decision of the Circuit Court of Appeals for the Second Circuit in the case of *Ben Ginsburg Co.*, supra. In the *Summerfield* case the Board adhered to its own line of decisions, calling attention to the split among the Circuit Courts of Appeals.

[5]*Crooks v. Harrelson*, 282 U. S. 55, 61 (1930); *United States v. Merriam*, 263 U. S. 179, 187-188 (1923); *United States v. Updike*, 281 U. S. 489, 496 (1930); *Reinecke v. Trust Company*, 278 U. S. 339, 348 (1929); *Bowers v. New York & Albany Lighterage Company*, 273 U. S. 346, 350 (1927); *Shwab v. Doyle*, 258 U. S. 529, 536 (1922); *Gould v. Gould*, 245 U. S. 151, 153 (1917); *Benziger v. United States*, 192 U. S. 38, 55 (1904).

WHEREFORE, your Petitioner respectfully prays that a writ of certiorari be issued out of and under the seal of this Honorable Court, directed to the Circuit Court of Appeals for the Fifth Circuit, commanding that Court to certify and to send to this Court for its review and determination, on a day certain to be therein named a full and complete transcript of the record and all proceedings in the case numbered and entitled on its docket, No. 6101, Woolford Realty Company, Inc., Appellant, v. J. T. Rose, Collector of Internal Revenue for the District of Georgia, Appellee, and that the said judgment of the Circuit Court of Appeals for the Fifth Circuit may be reversed by this Honorable Court, and that your Petitioner have such other and further relief in the premises as to this Honorable Court may seem meet and just; and your Petitioner will ever pray.

WOOLFORD REALTY COMPANY, INC.

By W. A. SUTHERLAND,

Counsel for Petitioner

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1931

WOOLFORD REALTY COMPANY, INC., PETITIONER,

v.

J. T. ROSE, COLLECTOR OF INTERNAL REVENUE FOR THE DISTRICT OF GEORGIA

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

I

The Opinions of the Courts Below

The opinion in the Circuit Court of Appeals for the Fifth Circuit, which was rendered on November 13, 1931, has not yet been printed in the Federal Reporter. The opinion is printed at pages 17 to 24, inclusive, in the record. The opinion of the District Court for the Northern District of Georgia is reported at 44 F. (2d) 856.

II

Jurisdiction

1. The jurisdiction of this Court is invoked under Section 240 of the Judicial Code as amended, United States Code, Title 28, Section 347.

2. The date of the judgment to be reviewed is November 13, 1931 (R. 25).

III

Statement of the Case

A full statement of the case is given under heading "A" in the foregoing petition and, in the interest of brevity, the statement is not repeated here.

IV

Specification of Errors

1. The Circuit Court of Appeals erred in finding and holding that a statutory "net loss" (within the meaning of Section 206 of the Revenue Act of 1926) incurred by a corporation in one year (1925 and 1926), when not affiliated, may not be used to reduce consolidated net income (within the meaning of Section 240 of the Revenue Act of 1926) of an affiliated group, of which such corporation is a member, in a subsequent year (1927) in which the corporation which has sustained the "net loss" does not have gross income in excess of the deductions allowed by Section 234(a) of the Revenue Act of 1926.

2. The Circuit Court of Appeals erred in affirming the judgment of the District Court sustaining the general demurrer to the petition.

V

Argument

The argument herein will follow the order of the reasons for the allowance of the writ set forth in the petition.

1. THE CIRCUIT COURT OF APPEALS IN THIS CASE HAS ERRONEOUSLY DECIDED AN IMPORTANT QUESTION OF FEDERAL LAW WHICH HAS NOT BEEN, BUT SHOULD BE, SETTLED BY THIS COURT.

The first reason for the allowance of the writ stated in the petition shows the question involved and the importance of a decision by this Court thereon. The statement of that reason is

not repeated here. While no attempt is made in this brief to present a thorough argument on the merits of Petitioner's contentions, a brief analysis of the pertinent statutory provisions is made for the purpose of presenting clearly the question involved and the importance of a decision thereon by this Court.

The question in this case involves the determination of consolidated net income. We discuss first the provisions for the determination of the net income of a single taxpayer.[6] The determination of consolidated net income is absolutely dependent upon these provisions.

Section 232 provides:

> "Sec. 232. In the case of a corporation subject to the tax imposed by section 230 the term 'net income' means the gross income as defined in section 233, less the deductions allowed by sections 234 and 206, . . ."

Section 234(a) provides:

> "Sec. 234(a). In computing the net income of a corporation subject to the tax imposed by section 230 there shall be allowed as deductions:"
>
> [There are then listed, under sub-paragraphs (1) to (11), all deductions permitted in determining net income, except "*net losses*" brought forward from preceding years, which is covered by Section 206].

Section 206(a) provides for the determination according to peculiar statutory provisions of what that Section designates as a "net loss." That the "*net loss*" defined in Section 206(a) is a statutory concept and not to be confused with *loss* in general, is made clear by Article 1621 of the Regulations, which provides:

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[6]All pertinent provisions of the Statutes and Regulations are quoted at length in an appendix to this brief. Throughout this brief references to Section and Article numbers relate to Sections of the Revenue Act of 1926 and Articles of Regulations 69, unless otherwise indicated.

"Art. 1621. . . . The amount properly allowed (as a 'net loss') may be neither the loss reflected by the return filed for the purpose of the income tax nor the net loss shown by the taxpayer's profit and loss account, but is to be computed according to the statute. . . ."

Section 206(b) with reference to the deduction of these statutory "net losses" from gross income in succeeding years provides:

"Sec. 206(b). If, for any taxable year, it appears upon the production of evidence satisfactory to the Commissioner that any taxpayer has sustained a net loss, the amount thereof shall be allowed as a deduction in computing the net income of the taxpayer for the succeeding taxable year (hereinafter in this section called 'second year'), and if such net loss is in excess of such net income (computed without such deduction), the amount of such excess shall be allowed as a deduction in computing the net income for the next succeeding taxable year (hereinafter in this section called 'third year'); the deduction in all cases to be made under regulations prescribed by the Commissioner with the approval of the Secretary."

Section 240(b), covering cases where corporations are affiliated and a consolidated return is filed, provides:

"Sec. 240(b). . . . the total tax shall be computed in the first instance as a unit and shall then be assessed upon the respective affiliated corporations (in the proportions provided). . . ."

Article 635 of Regulations 69, promulgated under Section 240, eliminates intercompany transactions and provides:

"Art. 635. Subject to the provisions covering the determination of taxable net income of separate corporations, . . . the consolidated taxable net income shall be the combined net income of the several corporations consolidated. . . ."

A mere reading of the provisions of the statute and regulations with reference to the determination of consolidated net income would seem to make it too clear for argument that the net income of a consolidated group is to be computed by taking the aggregate of the gross income of each member of the group and subtracting from this aggregate gross income the aggregate of all the deductions provided for each member of the group. Article 31(a) of Regulations 75, promulgated under substantially similar provisions of the Revenue Act of 1928, expressly provides that consolidated net income is to be determined in this manner.[7]

It is not disputed in this case that Petitioner and Piedmont Savings Company were not affiliated during the years 1925 and 1926, when "net losses" were incurred by Piedmont Savings Company, and for the year 1927 were affiliated and were authorized to and did make a consolidated return of net income for the purpose of taxation under the Act. And it is not disputed that the gross income of Piedmont Savings Company for the year 1927 was $453.80 less than the deductions allowable to it by Section 234(a).

The Circuit Court of Appeals has recognized the propriety of subtracting from the aggregate gross income of the two corporations all of the deductions allowable to each of the members of the group by Section 234(a), notwithstanding the fact that the aggregate of the deductions allowed on account of the Piedmont Savings Company by Section 234(a) was in excess of its gross income. But the Court has denied the propriety under such circumstances of deducting from gross income the "net loss" deductions of Piedmont Savings Company allowed

[7] "Reg. 75, Art. 31(a). *Definition.* Except as otherwise provided in these regulations, the consolidated net income of an affiliated group, which makes or is required to make a consolidated return for any taxable year, shall be the aggregate of the gross income of each of the members of such group less the aggregate of the allowable deductions of each of such members, except that gain or loss will not be recognized upon transactions between members of the group (referred to in these regulations as 'intercompany transactions')." (Cf. Rev. Act. 1928, Sec. 141.)

by Section 206(b). There is no basis whatever for making any distinction in a consolidated return between the deductions allowed by Section 234(a) and those allowed by Section 206(b). If the former deductions are permitted when in excess of the gross income of the separate corporation sustaining same, the latter must likewise be allowed.

From the opinion as a whole it seems that the Court reaches its decision adverse to Petitioner's contention upon the theory that the construction for which Petitioner contends would accomplish an inequitable result and a result "generally inappropriate to the Federal scheme of income taxation designed as it is *with the sole exception of the statutory net loss provision* to make each person subject to tax pay taxes on his income for the year in which it accrues." (R. 20.) (Italics ours.) This brief does not permit a full analysis of the error of this view. The fallacy of the assumption upon which this holding is based is clearly established by the fact that in Article 41(c) of Regulations 75, promulgated under substantially similar provisions of the Revenue Act of 1928, the Commissioner and Secretary of the Treasury expressly permit the deduction which Petitioner here contends is allowable.[8] The error of the Court's approach to the question is more fundamental. This is discussed under heading 3, page 20, infra.

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[8]"Art. 41(c). *Net Loss Sustained by Separate Corporation Prior to Consolidated Return Period.* A net loss sustained by a corporation prior to the date upon which its income is included in the consolidated return of an affiliated group (including any net loss sustained prior to the taxable year 1929) shall be allowed as a deduction in computing the consolidated net income of such group in the same manner, to the same extent, and upon the same conditions as if the consolidated income were the income of such corporation; but in no case in which the affiliated status is created after January 1, 1929, will any such net loss be allowed as a deduction in excess of the cost or the aggregate basis of the stock of such corporation owned by the members of the group."

It should be noted that the limitation of the net loss deduction to the cost to the affiliated group of the stock in the corporation which sustained the net loss prior to affiliation has no application whatever to any case where the affiliation occurred prior to January 1, 1929, the regulations being promulgated on January 3, 1929.

The language in some portions of the opinion of the Circuit Court of Appeals seems to indicate that the Court assumes that the literal language of Section 206(b), to the effect that the net loss deduction is to be allowed in the succeeding year in computing "the net income of the *taxpayer*" (Italics ours), requires that this deduction be limited to the individual taxpayer which sustained the loss. It could be argued with as much reason that the ordinary deductions allowable under Section 234(a) cannot be used in the computation of consolidated net income because Section 234(a) provides that "in computing the net income of *a corporation* subject to the tax imposed by Section 230 there shall be allowed as deductions" (Italics ours) the items there listed. An argument that the literal words of either section do not provide for the allowance of these deductions in the computation of consolidated net income would be clearly erroneous. Of course Sections 234(a) and 206(b) refer to single taxpayers. But Article 635, promulgated under Section 240, which provides that the income of the consolidated group shall be "the combined net income of the several corporations consolidated," necessarily means that all the items of gross income and all the deductions of the individual taxpayer must be taken into account. Otherwise it means nothing, and leaves to the Commissioner's caprice in each individual case, or to the individual opinion of whatever Court happens to be considering the matter, the determination of what, and under what circumstances, deductions are or are not allowable in a consolidated return. Section 240 and Article 635 expressly provide for the extension and enlargement of the provisions of the Act relating to the gross income and deductions of single taxpayers to make them applicable to an affiliated group. They do not leave the Commissioner or the Courts any more latitude in saying which of the particular deductions granted by statute shall be allowed to the consolidated group than they leave the Commissioner or a Court to say what deductions shall be permitted to a single taxpayer.

In other portions of the opinion it is intimated that Petitioner's contention requires the concept of "net income" as a minus quantity. Such is not the case if the provisions of Article 635 are interpreted, as we interpret them, as providing for the computation of consolidated net income by deducting from the aggregate of the gross income of the several corporations the aggregate of the deductions allowable under Sections 234(a) and 206(b). If, however, Article 635 is taken to require the computation of net income for each separate corporation, and then the combination of these separate net incomes, the concept of net income as a minus quantity is necessary. "Net income" as used in the Act *is a creature of statute* and is fully defined in Section 232. We find no difficulty in admitting the concept of net income as a minus quantity. It will always be a minus quantity when the deductions allowable by Section 234(a) or Section 206(b), or both combined, exceed gross income as defined in Section 233. In this case the Commissioner himself has allowed a minus figure, (which, upon this theory, must be *minus net income*) for the Piedmont Savings Company, to be combined with the plus net income of Petitioner in arriving at consolidated net income. The Court and Commissioner have refused to permit this minus figure to be increased by the deduction allowable under Section 206(b). (See page 13, supra.)

2. THE DECISION OF THE CIRCUIT COURT OF APPEALS IN THIS CASE IS IN CONFLICT WITH THE DECISION OF ANOTHER CIRCUIT COURT OF APPEALS ON THE SAME MATTER.

In the case of *National Slag Co. v. Commissioner*, 47 F. (2d) 846 (C. C. A. 3rd, 1931), it appeared that the National Slag Co. was affiliated with the Quakertown & Bethlehem Railroad Company throughout the year 1924. These two corporations were not affiliated in 1922 and 1923, in which years the Railroad Company had sustained "net losses" within the meaning of Section 206(b) of the Revenue Act of 1924, which is identical with Section 206(b) of the Revenue Act of 1926. In

1924 the Railroad Company's gross income was less than the deductions allowed by Section 234(a). The question presented to the Circuit Court of Appeals for the Third Circuit in that case is stated in the opinion of that Court as follows:

> "The single question here is whether the net losses sustained by the railroad company in 1922 and 1923 are allowable as deductions in computing the net income on the affiliated return of the companies for 1924; or to put the concrete question in general terms, it is, whether corporations affiliated for the year 1924, but not affiliated prior thereto, may add the loss of a member of the group, sustained in 1922 and 1923 to the loss of the same member sustained in the year 1924 in determining the loss of such member that may be deducted from the gross income of the group for the taxable year, 1924."

The Commissioner had disallowed the deductions of the net losses of the Railroad Company for 1922 and 1923 on the ground that "such losses may not be used to reduce consolidated net income for the year 1924 since the Quakertown & Bethlehem Company had no net income in 1924 to absorb the losses of 1922 and 1923." The Board of Tax Appeals had sustained this action of the Commissioner and had disallowed these losses.

But the Circuit Court of Appeals pointed out that shortly after the decision of the Board of Tax Appeals in the *National Slag Co.* case, the Board of Tax Appeals decided the case of *Alabama By-Products Corporation*, 18 B. T. A. 919, in which case the Board expressly overruled its decision in the *National Slag Co.* case. After analyzing the applicable statutory provisions, the Circuit Court of Appeals for the Third Circuit came to the conclusion that "the deduction of the losses here in question, sustained in 1922 and 1923, come directly within the provisions of the statute which are plain, certain and unambiguous." That Court held, therefore, that the statutory "net losses" suffered by the Railroad Company in 1922 and 1923

should be used to reduce the consolidated net income in 1924 of the affiliated group, of which the Railroad Company was a member, although the Railroad Company suffered a further loss in 1924.

The decision of the Circuit Court of Appeals for the Third Circuit in the *National Slag Co.* case is directly in conflict with the decision of the Circuit Court of Appeals for the Fifth Circuit in the case at bar.

The Circuit Court of Appeals in this case has pointed out a difference between the facts of this case and the facts of the *National Slag Co.* case. But even the slightest examination of this factual difference will show clearly that it cannot be the basis of a legal distinction. The Court refers to the *National Slag Co.* case near the end of its opinion (R. 24), where the following remarks are made:

> "Whether the decision in the National Slag Co. case was or not correct, it did not decide the point before us. That case merely decided that since one Buckland had during the years in which the statutory net losses were sustained, as well as during the year of affiliation, owned both of the enterprises, the loss was really his loss, and the statute should be construed so as to give him the benefit of it."

In the first place, it cannot be supposed that the Circuit Court of Appeals for the Third Circuit intended to limit its decision to any question narrower than the question quoted above from its opinion. It is true that in the *National Slag Co.* case it appeared that during 1922 and 1923, when the Railroad Company sustained net losses, the same individual who owned the Railroad Company also owned the business which was later turned over to the Slag Co. when that Company was incorporated on January 1, 1924. But there is nothing in the statutes that would give any legal significance to this fact. Indeed the Circuit Court of Appeals for the Fifth Circuit has itself recognized, in a case decided after the case at bar, that this factual

element in the *National Slag Co.* case does not explain the conflict between the decisions of the two Courts. In the case of *Planters' Cotton Oil Co., Inc. v. Hopkins*, decided by the Circuit Court of Appeals for the Fifth Circuit on November 20, 1931, the Court expressly stated that the factual difference between the *National Slag Co.* case and the *Woolford Realty Co.* case could not be made the basis of a legal distinction. Judge Hutcheson, again speaking for the Court, in the *Planters' Cotton Oil Co.* case, says:

> "Were this a case as that one was (referring to the Woolford Realty Co. case), of corporate affiliation of interests theretofore distinct, brought about after the net losses had been sustained, we should dispose of this case by a mere reference to that opinion. Since, however, the differentiating facts appear here as they did in the case of National Slag Co. v. Com'r., 47 F. (2d) 846, that one person has at all times been substantially the owner of all of the stock in all of the companies involved, and the tax ultimately fell on him because he at all times owned all of the companies, in the Slag case two companies so owned having been consolidated, in this case five companies so owned having been created by carving three out of the two which had sustained the net loss, *it becomes necessary for us now to determine whether these differences of fact require a different legal conclusion. We do not think they do.*" (Italics ours.)

The Court, therefore, reached the same decision that was reached in the case at bar.

It is respectfully submitted that there can be no doubt that the decision of the Circuit Court of Appeals in the case at bar is in conflict with the decision of the Circuit Court of Appeals for the Third Circuit in the *National Slag Co.* case.

The case of *Commissioner v. Ben Ginsburg Co.*, decided by the Circuit Court of Appeals for the Second Circuit on Novem-

ber 2, 1931, is clearly recognized by that Court as being in direct conflict with the decision of the Third Circuit in the *National Slag Co.* case.

3. THE CIRCUIT COURT OF APPEALS HAS DISREGARDED THE CLEAR AND REPEATED HOLDINGS OF THIS COURT TO THE EFFECT THAT THE RULE REQUIRING ADHERENCE TO THE LETTER OF A STATUTE APPLIES WITH PECULIAR STRICTNESS TO TAXING ACTS AND TO THE EFFECT THAT SUCH STATUTES ARE NOT TO BE EXTENDED BY IMPLICATIONS BEYOND THE CLEAR IMPORT OF THE LANGUAGE USED AND MUST IN ALL CASES OF AMBIGUITY BE CONSTRUED MOST LIBERALLY IN FAVOR OF THE TAXPAYER.

The analysis of the question involved in this case, made under heading 1, supra, shows that the Court below construes the statute and regulations against the interests of Petitioner in order to reach what the Court considers to be a result in keeping with the general purposes and intent of the statute. (Page 14, supra.) This is in utter disregard of the uniform holdings of this Court to the effect that the rule, which requires that a statute shall be interpreted according to its language and not in accordance with what the Court conceives to be its general purpose and intent, applies with especial strictness to taxing statutes which are in all cases to be limited to the words of the statute and are not to be extended upon equitable considerations. *Crooks v. Harrelson*, 282 U. S. 55, 61 (1930); *United States v. Merriam*, 263 U. S. 179, 187-188 (1923). There is no excuse whatever for a violation of this rule when, as here, a literal construction produces no unreasonable result.[9]

---

[9]The decision of the Circuit Court of Appeals for the Fifth Circuit in this case, and especially the approach of the Court to the issue involved, is in striking contrast with the decision of the Circuit Court of Appeals for the Fourth Circuit in the case of *Burnet v. Moore Cotton Mills*, 49 F. (2d) 59, 61 (2) (C. C. A. 4th, 1931), where the reasoning of the Circuit Court of Appeals for the Fourth Circuit on an analogous question is directly in conflict with the reasoning of the Circuit Court of Appeals for the Fifth Circuit in this case.

In the worst view of Petitioner's case the language can only be said to be ambiguous. Certainly the language does not clearly support, and the Circuit Court of Appeals did not hold that it clearly supports, its position. Another rule of construction repeatedly and emphatically laid down by this Court would require that if the language is ambiguous any doubt should be resolved in favor of the taxpayer.[10] The Court has completely disregarded this rule.

The soundness of the principle (applied with particular strictness to taxing statutes) that effect is to be given to the language rather than the supposed purpose of Congress, is illustrated with particular force in the present situation, where the express regulations of the Commissioner, under a statute for present purposes altogether identical with the statute here in question, has expressly permitted in specific terms the identical deduction which the Circuit Court of Appeals for the Fifth Circuit in this case held to be "generally inappropriate to the Federal scheme of income taxation."

The error of the Circuit Court of Appeals in this respect alone would be quite sufficient to warrant this Court in granting certiorari; so that it may lay down again, with an emphasis which cannot be misunderstood, the proposition that Courts are to follow the language of taxing statutes and not their own conceptions as to what in a particular case would be in keeping with the general purposes which Congress had in mind. Had the mind of the Circuit Court of Appeals been disabused of this error, its decision would undoubtedly have been different.

CONCLUSION

It is respectfully submitted that the question of Federal law involved in this case is a most important one and should be settled by this Court. The increasing number of cases in which the lower Federal Courts and the Board of Tax Appeals are deciding this question demonstrate its importance. Conflicting

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[10]See cases cited in footnote 5, supra.

decisions of the Circuit Court of Appeals create an unsatisfactory situation in any case. Such a conflict is most unfortunate in a question of Federal Income Tax Law where uniform administration throughout the country is required. Moreover, in reaching its conclusion the Circuit Court of Appeals has, it is submitted, violated the rules that statutes, and especially provisions of statutes imposing taxes, are not to be extended by implication beyond the clear import of the language used, and that all provisions of Revenue Acts are to be construed most liberally in favor of taxpayers. It is therefore respectfully urged that this Court grant the writ of certiorari.

Respectfully submitted,

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APPENDIX

Statutes and Regulations Involved

Revenue Act of 1926, Section 232:

In the case of a corporation subject to the tax imposed by section 230 the term "net income" means the gross income as defined in section 233 less the deductions allowed by sections 234 and 206, . . .

Revenue Act of 1926, Section 234(a):

In computing the net income of a corporation subject to the tax imposed by section 230 there shall be allowed as deductions:

[There are then listed, under sub-paragraphs (1) to (11), all deductions permitted in determining net income, except "net losses" brought forward from preceding years, which is covered by Section 206. The deductions listed under Section 234(a) include ordinary and necessary expenses, interest and taxes paid, losses sustained, bad debts, dividends from domestic corporations, depreciation, obsolescence and depletion.]

Revenue Act of 1926, Section 206(a) and (b):

(a). As used in this section the term "net loss" means the excess of the deductions allowed by section 214 or 234 over the gross income, with the following exceptions and limitations:

(1) Deductions otherwise allowed by law not attributable to the operation of a trade or business regularly carried on by the taxpayer shall be allowed only to the extent of the amount of the gross income not derived from such trade or business;

(2) In the case of a taxpayer other than a corporation, deductions for capital losses otherwise allowed by law shall be allowed only to the extent of the capital gains;

(3) The deduction for depletion shall not exceed the amount which would be allowable if computed without reference to discovery value, or to paragraph (2) of subdivision (c) of section 204;

(4) The deduction provided for in paragraph (6) of subdivision (a) of section 234 of amounts received as dividends shall not be allowed;

(5) There shall be included in computing gross income the amount of interest received free from tax under this title, decreased by the amount of interest paid or accrued which is not allowed as a deduction by paragraph (2) of subdivision (a) of section 214 or by paragraph (2) of subdivision (a) of section 234.

(b). If, for any taxable year, it appears upon the production of evidence satisfactory to the Commissioner that any taxpayer has sustained a net loss, the amount thereof shall be allowed as a deduction in computing the net income of the taxpayer for the succeeding taxable year (hereinafter in this section called "second year"), and if such net loss is in excess of such net income (computed without such deduction), the amount of such excess shall be allowed as a deduction in computing the net income for the next succeeding taxable year (hereinafter in this section called "third year"); the deduction in all cases to be made under regulations prescribed by the Commissioner with the approval of the Secretary.

Revenue Act of 1926, Section 240(a) and (b)

(a). Corporations which are affiliated within the meaning of this section may, for any taxable year, make separate returns or, under regulations prescribed by the Commissioner with the approval of the Secretary, make a consolidated return of net income for the purpose of this title, in which case the taxes thereunder shall be computed and determined upon the basis of such return. If return is

made on either of such bases, all returns thereafter made shall be upon the same basis unless permission to change the basis is granted by the Commissioner.

(b). In any case in which a tax is assessed upon the basis of a consolidated return, the total tax shall be computed in the first instance as a unit and shall then be assessed upon the respective affiliated corporations in such proportions as may be agreed upon among them, or, in the absence of any such agreement, then on the basis of the net income properly assignable to each. There shall be allowed in computing the income tax only one specific credit computed as provided in subdivision (b) of section 236.

Regulations 69, Article 635:

Consolidated net income of affiliated corporations.— Subject to the provisions covering the determination of taxable net income of separate corporations, and subject further to the elimination of intercompany transactions (whether or not resulting in any profit or loss to the separate corporations), the consolidated taxable net income shall be the combined net income of the several corporations consolidated. Only one specific credit of $2,000, as provided in section 236(b) and article 591, shall be allowed the consolidated group, and this only in case the net income of the group does not exceed $25,000; but if such net income is more than $25,000, the tax imposed by section 230 shall not exceed the tax which would be payable if the $2,000 credit were allowed, plus the amount of the net income in excess of $25,000. In respect of the statement of gross income and deductions and the several schedules required under Form 1120, a corporation filing a consolidated return is required to prepare and file such statements and schedules in columnar form to the end that the details of the items of gross income and deductions for

each corporation included in the consolidation may be readily audited.

Revenue Act of 1928, Section 117(a) and (b):

[Section 117(a) of the Revenue Act of 1928 *defines* "net loss" under the 1928 Act and does not differ in any way here material from Section 206(a) of the Revenue Act of 1926, page 23, supra. Section 117(b) with reference to the *deduction* of "net losses" is identical with Section 206(b) of the Revenue Act of 1926, page 24, supra.]

Revenue Act of 1928, Section 141(a), (b) and (c):

(a) *Privilege to file consolidated returns.*—An affiliated group of corporations shall, subject to the provisions of this section, have the privilege of making a consolidated return for the taxable year 1929 or any subsequent taxable year, in lieu of separate returns. The making of a consolidated return shall be upon the condition that all the corporations which have been members of the affiliated group at any time during the taxable year for which the return is made consent to all the regulations under subsection (b) prescribed prior to the making of such return; and the making of a consolidated return shall be considered as such consent. In the case of a corporation which is a member of the affiliated group for a fractional part of the year the consolidated return shall include the income of such corporation for such part of the year as it is a member of the affiliated group.

(b) *Regulations.*—The Commissioner, with the approval of the Secretary, shall prescribe such regulations as he may deem necessary in order that the tax liability of an affiliated group of corporations making a consolidated return and of each corporation in the group, both during and after the period of affiliation, may be determined, computed, assessed, collected, and adjusted in such manner as clearly to reflect the income and to prevent avoidance of tax liability.

(c) *Computation and payment of tax.*—In any case in which a consolidated return is made the tax shall be determined, computed, assessed, collected, and adjusted in accordance with the regulations under subsection (b) prescribed prior to the date on which such return is made. Only one specific credit computed as provided in section 26(b), shall be allowed in computing the tax.

Regulations 75, Article 31(a):

Definition.—Except as otherwise provided in these regulations, the consolidated net income of an affiliated group, which makes or is required to make a consolidated return for any taxable year, shall be the aggregate of the gross income of each of the members of such group less the aggregate of the allowable deductions of each of such members, except that gain or loss will not be recognized upon transactions between members of the group (referred to in these regulations as "intercompany transactions").

Regulations 75, Article 41(c):

Net Loss Sustained by Separate Corporation Prior to Consolidated Return Period.—A net loss sustained by a corporation prior to the date upon which its income is included in the consolidated return of an affiliated group (including any net loss sustained prior to the taxable year 1929) shall be allowed as a deduction in computing the consolidated net income of such group in the same manner, to the same extent, and upon the same conditions as if the consolidated income were the income of such corporation; but in no case in which the affiliated status is created after January 1, 1929, will any such net loss be allowed as a deduction in excess of the cost or the aggregate basis of the stock of such corporation owned by the members of the group.